

*Behavioural
aspects of
financial
analysts
(Proposal for Contemporary
Concern Study)*

TERM IV

GUIDE

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Proposal for Contemporary Concern Study

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TITLE

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INTRODUCTION

The world of analysts and investors is full of numbers and models used for decision-making. But the decision-makers are human beings. So it is likely that some biases do creep in the predictions of analysts as well as in the decisions by the investors. Behavioural Finance tries to capture this aspect.

Various researchers have studied whether any bias exists in recommendation of analysts and different aspects of such biases of analysts. In "Tracking Analysts' Forecasts over the Annual Earnings Horizon: Are Analysts' Forecasts Optimistic or Pessimistic?" Scott A. Richardson, Siew Hong Teoh and Peter David Wysocki record their observation that analysts put up an optimistic earnings forecast at the beginning of the year and walk down it through out the year. The estimate just before the earnings announcement tends to be slightly pessimistic so that on earnings announcement the investors get a pleasant surprise.

The extent of such a walkdown in earnings estimate would also depend on various characteristic of the analyst firm, e.g. size of the analyst firm.

Also, logic suggests that the accuracy of the forecast of analyst should improve as the date of actual earnings announcement approaches. This would happen because of availability of more information. However, the pattern of improvement of earnings forecast might differ depending upon characteristics of analyst firm.

OBJECTIVE

The objective of this study is :

To find out, based on empirical evidence

1. How the walkdown in earnings estimate varies for large and small analyst firms.

2. How the earnings forecast accuracy improves and whether it differs for large and small analyst firms.

METHODOLOGY

We are using the published research papers on behavioural aspects of analysts to get an idea about some biases in the behaviour of analysts. We would use data from secondary sources such as I/B/E/S. We currently have an I/B/E/S CD-ROM dated March 1997, containing:

1. Earnings estimate published by analysts for various firms for a number of years
2. Actual earnings of the firms analyzed for the analysts.

We would use statistical tools for analysis of the data to test the hypotheses whether walkdown in earnings estimate and improvement in earnings estimate vary for large and small analyst firms.

We would contact some security analysts who would be able to throw some light on the explanation behind particular patterns in the analysts' estimation. We might test some other hypotheses depending upon what comes out of these hypotheses.

DELIVERABLES

After this study we should be able to conclude:

- Whether walkdown in earnings estimate varies depending upon the size of the analyst firm
- Whether improvement in earnings forecast varies depending upon the size of the analyst firm

At least one of these deliverables would be completed before the mid-term evaluation.

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